RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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Feb. 24, 1999 **LETTER 1272**

Feb. 12 DJIA 9274.89; PTI 5333; A-D Ratio +3.12
Feb. 19 DJIA 9339.96; PTI 5338; A-D Ratio +2.99
Dow Yield: 1.66%; Dow Price/Earnings: 23.6
Dow 144-day MA: 8917; Dow 34-day MA: 9257
Dow Times Book Value: 5.85; PTI 89-day MA: 5337
Percentage of Undervalued Blue-chips: 6%
Gold 34-day MA: 289

RABBIT: This is the Chinese **"Year of the Rabbit."** To refresh your memory, when a rabbit senses danger, he survives not by fighting but by -- running away.

PRICE ACTION: The most interesting price action at this point may be what's been happening with both the D-J Utility Average and the Treasury bonds. What's happening is that they've both been in downtrends. In the case of bonds, the obvious is that bonds have finally taken the explosion in the money supply seriously. It's clear that the Fed, facing world deflation, is "pressing the pedal to the metal" and allowing the money supply to run wild. A surging money supply is inflationary. And bond-holders have been protecting themselves, accordingly.

In the case of the Utilities, their big slide suggests more than just rising rates. Historically, the Utility Average has tended to top out a few months to as much as a year **ahead** of the rest of the market. The D-J Utility Average topped out last October 9 at a value of 320.51 -- it headed down from there. On January 29 the Utility Average plunged below its December low. Thus, the Utilities have given their warning. The best thing we can do is -- listen.

As far as the other Averages are concerned, the story remains the same -- a top out by the Transportation Average last April 16. A high of 9643.22 was recorded by the Dow on January 8. Then new highs by the S&P 500 and the Nasdaq (unconfirmed by the Dow) were recorded on February 1. In other words, a general hodge-podge of new highs and non-confirmations in what I consider a slowly gathering primary bear market.

PRIMARY TREND INDEX: Extraordinary action: on the huge 184 Dow surge of January 11, the PTI registered only a plus 3. On that day breadth was very poor, and incredibly, we saw 21 new highs and 104 new lows. I don't think I've ever seen a huge Dow rise (184 points) accompanied by five times as many new lows as new highs. The next day (Feb. 12) with the Dow down 84 points the PTI dropped 8 points, taking the PTI below its 89-day MA and thereby registering a **"sell signal."**

ADVANCE-DECLINE RATIO: This index traces the declining or advancing action of all the issues on the NYSE. The decline in the A-D ratio has been relentless. For a detailed discussion of the A-D action, see Questions and Answers on page 2.

THE PICTURE: Older subscribers undoubtedly remember my old axiom, an axiom that I repeated often during the last major market decline. I wrote that with the US and its citizens loaded with trillions of dollars of debt, the choice boils down to a single decision -- **"inflate or die."** Never has that axiom been more to the point than now. Today the world is facing massive over-capacity. Everybody is producing, everybody wants to sell their own production, everybody wants to sell everybody else. On top of that, the US stock market has grown into a huge, speculative "dividend-less bubble." And while all this is occurring, two-thirds of the globe is in, or near, recession. The central banks of the world are facing a critical decision -- **INFLATE OR DIE.**

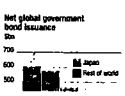
As subscribers know, the US has been doing its part to inflate -- and more. Now Japan, desperate to end its seemingly endless recession, is set to be the world's largest seller of government bonds. This year Japanese borrowing will account for an amazing 90% of all government bonds issued. Thus Japan has finally got religion, and that religion is **"inflate or die."**

Japan set to be world's top borrower

By Edward Luce in London — Government bonds flood is desperate bid to ward off depression

The Japanese government bond market is set to overtake the US Treasury market to become the largest in the world as a result of fixed income economist at J.P. Morgan. "This could have a far-reaching impact on bond prices around the leading net figure of $360bn.

Japan's issuance contrasts starkly with the position of the US government, which will reduce the outstanding value of could therefore have much further to rise. The crucial difference this year is that Japan's government is unlikely to buy large amounts of its own debt.



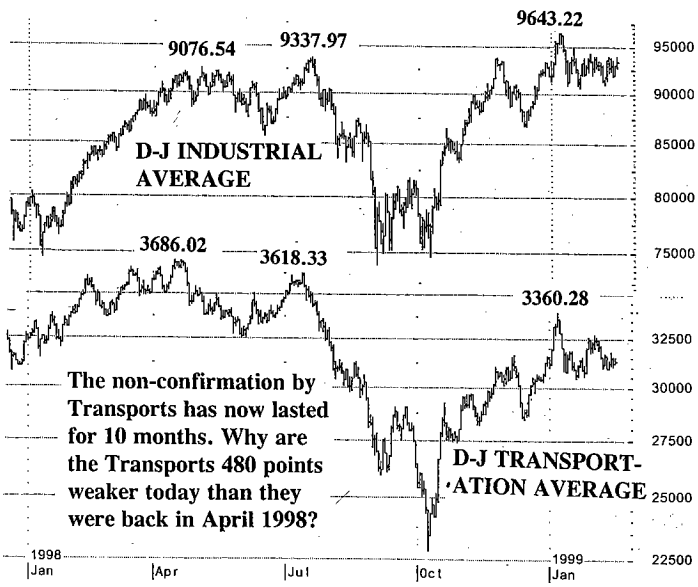
In the meantime, Brazil struggles with chronic currency problems, high interest rates and a recession (thereby pushing all of S. America to the edge). In Europe economies are shaky, with Germany, France and Britain all showing little or no growth. Unemployment across Europe remains in the 10% plus area. How long will it be before Europe faces the same choice -- inflate or die?

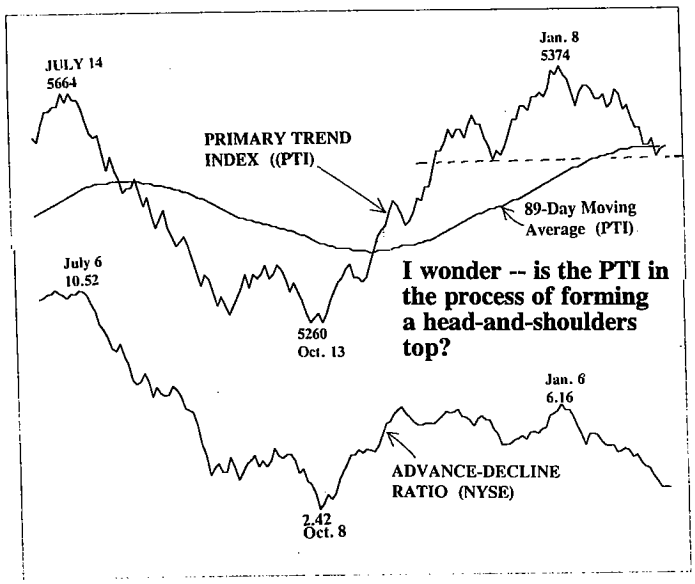
Europe's Outlook Dims With Britain's; Rate Cuts on Continent Appear Unlikely

By Silvia Ascarelli And G. Pascal Zachary
Staff Reporters of The Wall Street Journal
LONDON — Europe's growth prospects

Anxiety in the Euro Zone
Slowdown in Europe

That pretty well describes the current ongoing global battle. The world is producing too much. Too much = deflation. Deflation = dying, and central bankers are not about to allow their respective nations' economies to die. **Result** -- an avalanche of bonds coming out with a resultant pressure on interest rates. The great end-of-the-century economic war is on; it's called -- **"Inflate or die." Note:** On Feb. 16 the Bridge-CRB Commodity Index broke to a 24-year low while the Goldman Sachs Commodity Index sank within a fraction of a 26-year low. On the same day gold broke 4.80 while silver dropped 26 cents.





The questions are coming in thick and fast, and I'll try to answer some of them now.

Question: OK, Russell, so the world must inflate or die. But which side will win, the inflation side or the bear market, the deflation (dying) side?

Answer: Gee, how about an easy question? But seriously, since I believe a primary bear market is on, I have to doubt whether inflation is going to save the US or the world economies. In other words, the bear will win. But believe me, it's going to be one fierce battle. And the battle is just heating up (note our saviors, Fed chief Greenspan and Treasury Secretary Rubin on last week's cover of *Time* magazine).

Question: Last year during July to October the stock market got hit hard. You received a bear signal on August 4 -- and you announced a bear market under Dow Theory. How do you know that the bear market didn't end at the October lows?

Answer: The question is really whether last year's decline was just a correction in a bull market or whether it was the first leg of a primary bear market. I had to make that decision. Based on the non-confirmation by the Transports, based on severe overvaluation, based on heavy volume and speculative intensity, based on the prevailing wildly bullish sentiment, I took the August 4 action to be a **valid Dow Theory signal** -- a signal telling me that the tide had turned, and that a primary bear market was in force.

I also took into consideration the almost universal refusal by analysts, Wall Street experts and most stock market students to even entertain the idea that the great bull market was breathing its last. Of course, even today probably 95% of investors haven't the slightest suspicion that the great bull market has ended and that a primary bear market has arrived. This amazing ingrained bullishness is characteristic of sentiment at the end of a major bull market.

But already the bear can boast many victims. For instance, the following is from a Feb. 5 Merrill Lynch bulletin: *"About 32% of the S&P 500's component stocks, 48% of all NYSE common stocks and 67% of all Nasdaq common stocks were 30% or more below the highs they reached between January 2, 1997 and July 31, 1998 (the months when most stocks hit their post-1994 bull market peaks)."*

Question: Russell, if you are correct, if the bull market is indeed over and a bear market has started, how long and how far do you expect this bear market to carry?

Answer: I thought I went over that in the last Letter. At any rate, if this is indeed "the big one" I would expect it to last for at least a few years and to take the major averages back to the point where yields are again attractive to serious investors. This could mean average yields on the Dow of anywhere from 5-6% to possibly considerably better than 6%. To get to a 6% yield, the Dow would have to drop to the 2500 range. Consider this -- if the Dow was to drop to just a 3% yield (remember, 3% used to be the "danger area"), the Dow would have to decline to the 5000 range. Could anything like the above happen? Certainly it could. Remember, "the market can do anything."

Question: You've written a lot about the advance-decline ratio, and you've taken its action as bearish. Explain.

Answer: The decline in the A-D ratio, beginning on April 3 of 1998, has been extraordinarily persistent. In fact, **the most persistent action in this market over the last 10 months has been the declining breadth.** Now this is very important. Let's say the A-D continues to decline, and it breaks below its October 8 low of 2.42. And let's say the Dow refuses to confirm in that the Dow refuses to break below its own October low of 7632.53. In a bull market, I would take that non-confirmation by the Dow to be constructive, and I would expect a good rally to follow such a non-confirmation.

But in bear market (as now) I would expect the A-D ratio to **lead the Dow.** In other words, in the present case, if the A-D ratio breaks below its October low, I would expect the Dow (in due time) to **confirm** by breaking below its own October low of **7632.53. (Be sure to see Late Notes on page 6 for the latest on the A-D ratio, the PTI and the market.)**

Question: The Fed is flooding the US and the world with dollars. How can we have a bear market with this kind of roaring liquidity?

Answer: The bottom line is that the Fed can't control the primary trend of the market and neither can anyone else. Nobody knows that better than Greenspan. After all, it was Greenspan who warned the authorities (and Clinton) that the Social Security Trust Fund should stay out of the stock market. As to the flood of dollars, ironically, the Fed's dollar flood could even turn out to be a negative force for the market in that it will encourage **additional global capacity** -- when the last thing the world economy needs is more capacity.

Question: Russell, you began the last Letter warning about global deflation. But if the Fed continues to flood the world with dollars, how in the world are you going to get deflation?

Answer: The Fed can print dollars by the billions, but if the bear really takes hold, if the stock market heads down in earnest, at some point people are going to get scared. And when they get scared they're not going to spend [remember, savings are now negative (below zero) in the US]. At some point, as fear takes over from bullishness, people are going to decide to save. When that happens, watch out.

A bitter example: when I was a teenager during the Great Depression my father, a life-long real estate man, tried to interest investors in buying brownstones (individual houses) in midtown Manhattan on the favored East Side. At the time (1939-1942) they were literally giving brownstone buildings away (these same buildings now sell in the millions). But in those days, nobody would put up the money. People were just plain frightened. You could have bought a brownstone building on Third or Second or First Avenue in Manhattan for $20,000 down: the buildings were throwing off a return of 30% and were only half-occupied -- and nobody, nobody would put up the cash. Talk about refusing to part with your money, I saw it. I saw it first-hand. I was there, and it was amazing and depressing.

The point I'm making is that psychology, sentiment, changes during a severe bear market. Actually, we're seeing some of that in Japan today. The money is available but the Japanese people are afraid to spend. Unemployment has climbed to 4.1% in Japan, but the Japanese grew up believing that their jobs were guaranteed for life. Unemployment scares the hell out of the Japanese, and for the first time in their lives they're seeing unemployment. Result -- the Japanese are saving even more than usual, rather than spending, this despite the fact that money is freely available and their government is begging them to spend.

Question: Russell, what signals are you looking for to tell you that the bear market might be moving into a higher gear?

Answer: I guess the first thing I would look for is the Dow closing below the **9100** level. The next thing I'd look for is the Dow breaking below its December low of **8694.60.** As you know, the advance-decline ratio and the Utility Average have already broken below their December lows. I doubt that the market would take kindly to the Dow breaking below its December low.

But I'll remind subscribers that the public and the great majority of professionals remain remarkably bullish. It's a bullishness that's been built up over many years. That kind of bullishness will not be dissipated in a few weeks or even a few months of bear market erosion. It's going to **take time.** But the bear's got time, all the time in the world.

Question: I note that the advance-decline ratio continues to erode, but the Dow and the S&P stubbornly resist the decline. What does this mean?

Answer: Imagine you are a fund manager. Public money keeps coming into your fund, and you've got to spend that money. You know that the great majority of stocks are declining, so you are afraid to buy them. Therefore, you go with what seems "safe," and you go with stocks that have huge liquidity, and you go with stocks that are rising or at least holding up. This narrows your choices to maybe 100 big-cap stocks -- and that's where the money is going. This phenomenon is what's keeping this extraordinary party going -- the disparity between a limited number of big-cap stocks and the rest of the market. Ultimately, whatever is driving the majority of stocks down will move to the big-cap stocks. But it's taking time.

Question: The February 15 issue of *Time* magazine featured Fed Chief Greenspan, Treasury Secretary Rubin and Undersecretary Summers on the cover with the caption of how "the Three Marketeers have prevented a global economic meltdown -- so far." What did you make of this?

Answer: I read this long article carefully. And surprisingly, it didn't say a damn thing. I believe it was a plant (since it obviously had the cooperation of these three men). I also thought it was a puff piece, implying that Greenspan and the guys at the Treasury had the whole world economy in control, well, sort of. I will say this -- never has this nation placed so much confidence in the ability of the Fed to control the stock market and the US economy. Greenspan has become almost a god. But Greenspan's no fool; he knows in his gut that the primary trend of the market is beyond his or anyone else's control.

Question: What do you make of the near-term market action here?

Answer: On February 12 (a Friday) the PTI plunged 8 points. In doing so, it broke below its 89-day moving average. That break constituted a "sell signal" on the part of the PTI.

Interestingly, last year on April 4 (when the A-D ratio was at its peak) the PTI stood at 5352. That was roughly 20 points above where the PTI is now. In other words, the PTI has made no upside progress over the last 10 months. Other statistics: new 52-week lows are now half of what they were 10 months ago. Also, at latest count, only 29% of all NYSE issues are above their 200-day moving averages.

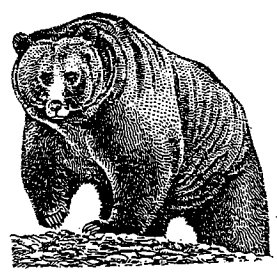
As far as the **big picture** is concerned, remember, according to my Dow Theory studies, the primary bear market started on **April 16, 1998.** And evidently, the same action that characterized 1998 is continuing into 1999. In other words, a limited number of tech and net stocks have surged, thereby masking the bearish action of the majority of stocks as measured by the advance-decline ratio. How long this ominous "parting of the ways" can go on -- I don't know, but like ol' man river, the divergences just keep "rollin' along."

In the meantime, we wait. Patience is a great virtue in this kind of market. The steady hype from talking heads on CNBC, FNN, the newspaper columns, the newspapers -- this hype, of course, is constantly aimed at "what stocks to buy." The public wants action and the media knows how to feed the fires. Buying and trading stocks has become the most popular game of the '90s, even with stocks now at the highest valuations in history.

The **BIG PICTURE** as I see it is this: I think most or all of the indices and averages have **put in their tops.** But with surging liquidity, many stocks are hanging on or even rallying, this despite the steadily declining breadth. This milling around, this gradual erosion, will probably continue until the economy is close to actually turning down or until something comes along to shatter the public's fanatic ingrained bullishness. In the meantime, this market will whip back and forth, keeping investors and traders hoping and keeping analysts guessing.

To cap the whole picture off, all that was needed was our leader, President William Jefferson Clinton, coming out in his State of the Union speech with a novel idea -- we'll load up the Social Security Trust Fund with stocks, thereby saving Social Security by harnessing it to the "almost guaranteed rising trend" in common stocks. Happily, Fed Chairman Greenspan (with whom, nobody argues) squelched that idea.

INVESTMENT POSITION: The bear inhabits the box. You really have three choices here. **(1)** You can sit with your stocks and funds (assuming you still have stocks or mutual funds) and simply watch the market -- hoping all the while that somehow everything will turn out well. **(2)** You can continue to buy stocks -- and try to beat the bear. **(3)** You can stay out of the market and watch your friends and neighbors try to beat the bear.



I'll make this section short and sweet. I recommend position number 3. In the end it will probably save you a lot of anxiety and money. Anxiety is very hard on both your psyche and your body. Monetary losses are just a plain bummer.

Where should you park your money? Preferably in T-bills.

NOTES & QUOTES: I'm now putting daily PTI readings on our new website along with my daily market comments and observations. I'm really hoping that ALL my subscribers avail themselves of this new free service -- but it does entail your having a computer and learning how to get on the net. I know there is probably a certain percentage of my subscribers who

don't have a computer, but listen, here's your incentive to go out and buy one (they're cheap now) and well, move into the twenty-first century. Believe me, learning "computer-ese" is not that difficult. It's fascinating, it's modern, and it will open up a whole new world for you. I graduated from Smith Corona typewriters to computers about 10 years ago, and that was one of the best and most rewarding things I ever did. So c'mon, you reluctant old-timers, go out and buy a computer and get on the net -- so I can talk to you every day. **Note:** to get your user name plus the password which will allow you to get on my **www.dowtheoryletters.com** website, you have to go to the website by entering our web address on the address line and the home page will come up. You then sign up for your user name and password in the **web sign up** section. By the way, you can pick any word, group of numbers, or phrase for a "user name" and "password," but be sure to **remember** the phrases you pick because we won't repeat them in our confirmation to you when your access to the member services is set up. (Please note: these phrases are "case sensitive" which means that if you request something in all caps, all lower case, or mixed, that is **exactly how we will enter them into our program, and exactly how you will have to enter them to access member services once we have processed your request.)** Finally, if you need help with all this, call our resident computer genius, Lynn Hunter; she's harried, but she'll be happy to walk you through the process. You can do it! **Patience**: We're getting hundreds of requests every day from subscribers who want to get on our website. Sorry, we can't get to you on the same day, but we're going **as fast as we can.** Patience, please!

* *

Speaking of the net, which are the most "wired" cities -- or the cities with the highest percentage of population on the net? (1) San Francisco; (2) Austin, TX; (3) Seattle; (4) Wash., DC; (5) Boston; (6) San Jose, CA; (7) San Diego; (8) Minneapolis-St. Paul; (9) Atlanta; (10) Dallas-Ft. Worth.

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Mighty Microsoft has its troubles. MSFT is doing poorly in court, and according to the *WSJ* (Feb. 18), its high-toned NY law firm, Sullivan and Cromwell, is, er, screwing it up. CEO Gates also made a lousy witness. On top of that, a competing operating system, Linux, has some real backing via IBM, which is now offering the Linux system on a range of its computer servers, work stations and personal computers.

* *

The collapse in commodities has been, and is, breath-taking. Everything has hit the skids -- cotton, oil, gasoline, cocoa, soy beans, wheat, oats, orange juice, sugar; I haven't seen anything like this in decades. They call it deflation. The following from a front page article in the Feb. 18 *NY Times*: "Mr. Burrus, a 65-year-old, has seen some tough times in a life of hog farming, including a fire that ripped through his barns in 1978 roasting 1200 pigs alive. But nothing, he said, has ever been nearly so devastating as today's prices. These days he is bleeding money so badly that he worries about losing his 600-acre farm 130 miles southwest of Chicago. 'This is something we've never seen in the livestock business,' Mr. Burrus said dolefully. 'We've never seen this heavy a loss in the pork industry, not even in the Depression.'"

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Well, the "Comeback Kid" has escaped again. But his moral authority (not that he ever had very much) has been destroyed, and it's doubtful whether he will be able to get much done over the next two years. Furthermore, if the bear market kicks in, I would bet that Clinton's vaunted popularity will sink like a stone. It's generally conceded that Hillary, in sticking by the Prez, saved him from banishment. From here on, what Hillary will do (her commodity rip-off and her disastrous "health plan" have now been forgotten) will probably generate more interest than anything Bill might do (unless, of course, Bill gets into more trouble). It's clear that Hillary is a power-freak and it's certainly possible that she'll run for a Senate seat out of NY (although some New Yorkers are already calling her a "carpetbagger"). Personally, I'd love to see the last of both of the "poison pair" by the end of Clinton's term of office -- but I'm afraid that's not to be. **Note:** Experts are saying that the Republicans have destroyed themselves in trying to rid the nation of Clinton, but a lot of thinking and sentiment will change if the bear enters the picture.

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The world auto industry can produce 80 million cars if they have to. But the market only wants maybe 45 million cars. So what's happening is consolidation and mergers. Ford bought Jaguar and is thinking about buying Volvo. Daimler Benz bought Chrysler and is thinking about Nissan. The rumor is that BMW is for sale. It's a new world out there, and the auto industry knows it.

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Jim Grant (*Grant's Interest Rate Observer*, 30 Wall St., NY, NY 10005) notes that even the Swiss, of all people, are now inflating. The year-over-year change in Swiss National Bank assets are now running between plus 19% to plus 25%. Wow!

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Many months ago in this section I opined that the future for all things electronic was probably going to be **wireless.** I pointed to my satellite TV, which I put in when the little 18-inch dishes first became available. I then asked the question, "Why are companies spending billions on cable when it seems to me that wireless is the wave of the future?" One answer was that these companies wanted to get into the swim immediately and wireless just wasn't available at the time. A second is the big drawback with wireless -- it's not two-way (at least so far). In other words, you can only receive information.

Nevertheless, times are changing, and rapidly. And slowly but surely, the tech world is going wireless. I include two clips from the February 8 *WSJ* in proof of the above. As I see it, it's only a matter of time. Finally, imagine the Internet on wireless, allowing it to be "broadcast" to every nook and corner of the world.

Sales Surge for Wireless-Phone Makers

Dataquest Says Unit Sales Increased by 51% in 1998 As Nokia Took the Lead

By Quentin Hardy And Gautam Naik
Staff Reporters of The Wall Street Journal

The fight goes to the Finnish.

Makers of wireless phones sold a record 162.9 million units world-wide last year, a 51% increase from 107.8 million units, as has a wholesale price of slightly more than $170, valuing the market at more than $27.7 billion last year. Service providers often discount the phones to sign on people to their service contracts, making these phones seem cheaper at retail.

"There was some really explosive growth in the market," said Peter Richardson, who wrote the report. Among the key markets, he said, European service providers did well through sales of prepaid wireless services, and Japanese consumers bought new styles of phones despite that country's economic troubles. In the U.S., new plans offering cheaper calls over more of the country led to massive fourth-quarter purchases

the market, up 52% from 20.6 million units, a 19% share, in 1997. Motorola sold 32.3 million units for a 20% share, up 28% from 25.3 million units, or a 23.5% share, in 1997. Sweden's Telefon AB L.M. Ericsson was third, with 23.8 million wireless handsets sold, a 15% share, up 50% from 15.9 million units, or 15% of the market.

Officials at several of the companies in the report confirmed its general outlines. "It might be at the high end, but it is not far off," said Jan Ahrenbring, vice president of marketing at Ericsson. "About 15% would be right" for Ericsson's market share, he said, adding that his company expects more than 200 million number of phones it sells or its market share, but Mr. Calle acknowledged, "We gave up some share, particularly in the early part of the year."

Motorola underwent a massive reorganization last year in hopes of becoming more customer-oriented. The Schaumburg, Ill., company recently released a large variety of phones and is working on accessories such as an electronic organizer

Motorola, Cisco Systems to Work Jointly On Wireless Services for the Internet

By Scott Thurm And Quentin Hardy
Staff Reporter of The Wall Street Journal

Motorola Inc. and Cisco Systems Inc.

networking by May. They hope to create a world where the operators of wireless networks can use interchangeable equipment based on standards, instead of the

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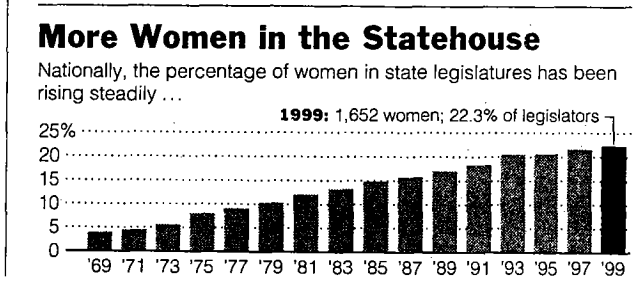
Speaking of the future, I continue to predict that the wave of the future is -- **women.** The statistics are amazing. In 1961, 224,538 men received bachelor's degrees from US colleges vs. only 140,535 women. This year 532,000 men will receive bachelor's degrees from US colleges compared with (get this) 735,000 women. In almost every area of studies from law to medicine, women are moving up and actually outnumbering men. But the real power lies in the political arena. So check this chart. In

STATUS REPORT

More Women in the Statehouse

Nationally, the percentage of women in state legislatures has been rising steadily ...



some states such as Washington, Nevada, Arizona, up to 40% of the pols in state legislatures are women. In California, Oregon, Colorado, Nebraska, Kansas, Minnesota, 25-30% of the pols are women. And the latest -- it's almost certain that Elizabeth Dole will be running for President. Surprise -- recent polls show that a Bush-Dole ticket would beat an Al Gore ticket by a wide margin.

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Analysts continue to dissect the stock market action of 1998. The real action last year was in the S&P 500, not the Dow. But pertaining to the S&P, analysts at Salomon Smith Barney came up with some extraordinary statistics as follows: last year just 10 stocks accounted for 43% of the gain in the S&P, 25 stocks accounted for 67% of the gain and 33 stocks accounted for over 75% of the gain. Even more extraordinary -- two-thirds of all US stocks **actually declined** during 1998. In the end, said Salomon, 1998 will be remembered as the year "the largest stocks had a really big performance party, and everyone else stayed home." Merrill Lynch's analysts point out this amazing statistic: almost half (48%) of all NYSE stocks are down 30% from whatever highs they hit during '97 or '98. This suggests that many traders and investors are now losing money. Also, these wild, erratic market moves are very tough on traders. The market surges for a day or so and kills the shorts. Then it drops violently and it kills the longs. It's an unbelievably difficult market for traders and especially for the so-called "day-traders" on the net.

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Japan's Nikkei stock average is hanging around 14000 again. What's wrong? As *Business Week* (Feb. 15) puts it, "Japan's trillions are a far weaker bulwark against change than anyone has imagined. Japan is running out of money to prop up its bankrupt banks and companies and absorb at least $600 billion in bad loans. The only solution is to weed out weak companies and invite in foreign capital . . . Yet the fear is that the government cannot continue to bail out sick companies. Prime Minister Obuchi's government thinks it can readily raise $500 billion for fixing the banks and earmark another $200 billion in easy credit to companies, tax breaks to consumers and public works . . . Yet raising that money could prove prohibitively expensive." **Russell Comment:** Let me put it succinctly, Japan is still facing a huge amount of problems. And Japan's "mandarins" don't want reforms. The latest is that the Bank of Japan now has to decide whether to take the last desperate measure, and that is monetizing the debt (inflation) by buying Japanese government bonds. With a very large percentage of Japan's aging population on fixed income, inflation in Japan would be intolerable and politically extremely dangerous.

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By the end of this year Japan's bond market will pass the US bond market in total size, making Japan the "bond-king" of the world. Writes the *WSJ* (Feb. 9), "In the short run, analysts predict that Japan's voracious appetite for cash will devastate an already bruised Japanese government bond market as prices sink and yields rise." This year nations will issue $390 billion of new bonds, but the staggering fact is that 90% of those new bonds will come from Japan. **Russell Comment:** As Japanese bond yields rise, there will be less reason for the Japanese to buy US bonds for higher yields. One Japanese bond expert opines that the Japanese long bonds will hit a yield of 4% by the end of the year.

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	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/3) $/troy oz.	286.850	283.800	-3.8
STEEL SCRAP (2/2) #1 heavy, $/ton	84.00	84.00	-42.3
COPPER (1/29) ¢/lb.	68.0	69.2	-10.5
ALUMINUM (1/29) ¢/lb.	59.0	59.3	-19.7
COTTON (1/29) strict low middling 1-1/16 in., ¢/lb.	57.76	57.54	-7.3
OIL (2/2) $/bbl.	12.04	11.86	-25.4
CRB FOODSTUFFS (2/2) 1967=100	200.24	205.92	-11.9
CRB RAW INDUSTRIALS (2/2) 1967=100	262.14	262.80	-11.7

Following up on "Global Deflation" as put forth in the last Letter, this run-down from *Business Week* shows the yearly changes in basic commodities. Deflation often begins with swings in commodity prices.

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When historians want to document the excesses of the great boom of the early '90s, what examples will they use? Will they use New York restaurant prices or will they use San Francisco housing prices or maybe the price of a lady's crocodile hand-bag ($5,000) at Saks Fifth? Nah, they'll probably use the price of a sports franchise. In 1998 the Texas Rangers sold for $250 million and the LA Dodgers sold for $360 million and the Cleveland Browns sold for $530 million. The topper came in '99 when the Washington Redskins sold for $800 million. Now the rumor is that LA will get an NFL franchise, but the price may be around $1 billion (hopefully they'll throw in a stadium).

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Incidentally, this story from the Feb. 9 *LA Times* tells us that California is now featuring million-dollar tract homes, and furthermore, these million-dollar beauties are now being mass produced. Says the article, "No fewer than 30 subdivisions -- albeit gated ones -- with prices in the $1 million range are under construction across the Southland, with waiting lists as long as 200 names. Even cities not known for an abundance of affluence, such as Long Beach and Thousand Oaks, are seeing homes built in these lofty price ranges." **Russell Comment:** We can thank Greenspan and the money-supply explosion for this.

New California Dream: The $1-Million Tract House

■ **Real estate:** Sales of high-priced homes zoomed in '98. But a million doesn't get you what it once did.

By DARYL STRICKLAND
TIMES STAFF WRITER

Sales of homes worth $1 million or more in California soared to an all-time high last year as the state's come with swimming pools or ocean views. Many have only three or four bedrooms.

Meanwhile, million-dollar homes are becoming so commonplace that they are now being mass-produced.

* *

Poor Bill Gates. Last week he said he'd gladly give up all his money if the government and their trust-busters would just leave him and his company alone. On top of that, competitors keep worrying Bill -- with new threats such as Java and now Linux, the latter being another operating system that its creator is giving away free to assorted computer nerds. Two weeks ago it was announced that Gates gave away a few billions to charity. The announcement was legitimate, but to be honest Gates gave the money to two of his own foundations (aw, he just doesn't like to give up control).

* *

Entrepreneurs are still hitting pay-dirt by bringing out IPOs with a .com in the name. No less than 35 Internet-related firms have filed to sell stock in coming months. Writes the editor of *Forbes* magazine, "I've given up trying to understand why Amazon is worth $17 billion and Yahoo twice that. Now I'm trying to understand why their managers don't take advantage of the situation. Shouldn't they be selling stock? They could maybe raise a few billion in a second stock offering. Equivalently, they could use their high-priced shares to acquire some real assets, instead of just using them to acquire other airy Internet stocks." **Russell Comment:** Talk about flying billions of paper dollars, I've never seen anything like it.

* *

Jimmy "Big Boy" Valente, ex-pro wrestler, was the phenomenon of the recent voting. He's now governor of Minnesota. He's honest, he's a man, he's a maverick, he's totally out-spoken, and the voters LOVE him. Here's how Valente describes the Democratic party: "The Democrats started out with the New Deal, a good idea for its time, and then delusions of grandeur led them to keep adding on to it, like a guy who sets out to make carbonara sauce and starts throwing sausage and peppers and onions in, and pretty soon you've got hearts of palms and peas and anchovies and water chestnuts and

pineapples swimming around in it and the thyme and oregano are at toxic levels and nobody's hungry anymore. That's the Democratic platform. Programs for everything -- programs to combat grumpiness, stupidity, discrimination, covetousness, improper lane changes, low math scores, flat beer, poor taste and too much air in Cracker Jack boxes -- and all of the programs require battalions of social workers and reams of paper." (Next Letter, he describes the Republicans.)

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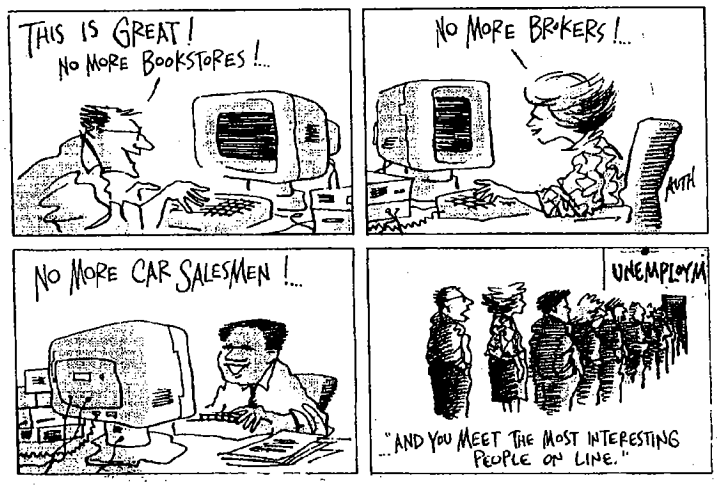
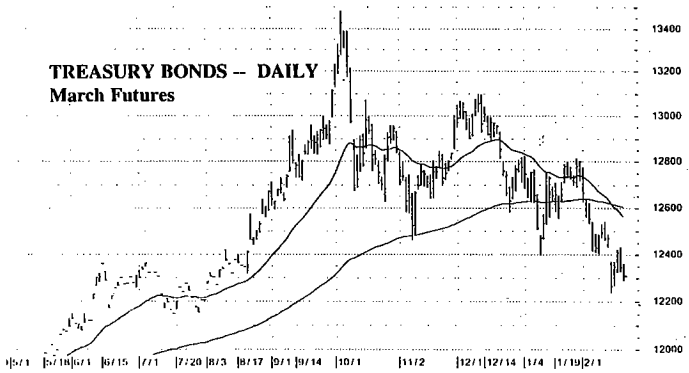
My "little old" alma mater, NYU, is now the largest private university in the nation. NYU has thousands of pages on the net, and the "hits" are doubling every six months. Applications for the freshman class have been booming with the University now accepting only 34% of applicants, down from 65% in 1991. NYU used to be a "subway" university, but half its students now come from outside the City. The percentage of freshman from the top 10% of their high school classes has risen from 42% in 1991 to 60% today. This is rather typical of "top-choice" colleges throughout the nation. There are so many colleges and divisions at NYU that I can't keep up with them. The catalogue of courses offered looks like the old Sears catalogue -- huge.


THIS IS GREAT! NO MORE BOOKSTORES!...
NO MORE BROKERS!...
NO MORE CAR SALESMEN!...
UNEMPLOYM
"AND YOU MEET THE MOST INTERESTING PEOPLE ON LINE."

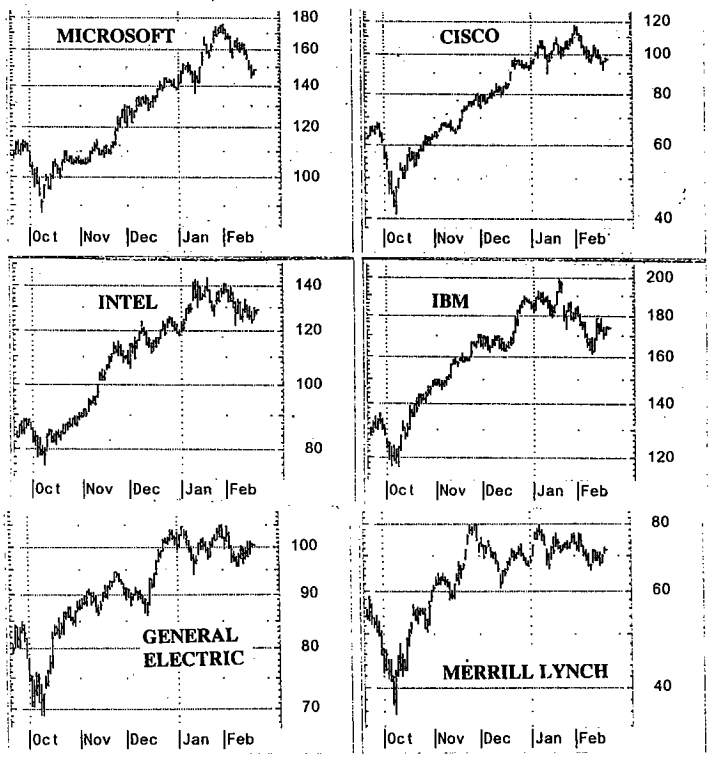
GOLD, BONDS, DOLLARS: One, two or three items will normally reflect the fact that the Fed is allowing the US money supply to run wild. I'm talking about gold, bonds and the dollar. So far, the bonds have been the only tell-tale item. But let's start with gold. I show below the **weekly** chart of gold, and what we are probably seeing here is a five-month bottom forming. The first hint of gold strength would be gold climbing above its 34-week moving average at 293, and then gold pushing above the 300 psychological level. I have to wonder what's keeping gold down in the face of the ocean of dollars being produced. Ah, the mysteries of the market.

The next chart is a **daily** chart of the March T-bond contract. Note that the 34-day MA has now dropped bearishly below the 144-day MA. The **bonds are in a bear trend,** and declining bonds exert pressure on stocks. The big question is whether bonds will continue to decline.



The dollar, not shown, remains strong. It's highly unusual and counter-intuitive to see a strong dollar and weak bonds. To be honest, I haven't figured this one out yet (has anybody?).

STOCKS: I'm including daily charts of six KEY stocks, stocks with huge capitalizations. First off is Microsoft, which topped out when it broke 155. Cisco is in a head-and-shoulders top. Intel is in a downtrend with its key level at 120. IBM is in a downtrend with its new support at 160. GE is a proxy for the whole US economy; its trend is neutral with critical support at 95. I have always considered Merrill as a bellwether stock. It's now trendless with first support at 66 and more important support at 60. These are six of the most popular and most watched stocks on the NYSE. None is at new highs and four of the six appeared to have topped out.



LATE NOTES: A quarter of a century of accelerating bullishness doesn't die easily. But then, I never thought it would . . . The PTI action (page 2) is particularly fascinating. The area around 5337 was touched in mid-December and again last week -- a slight break of the 89-day MA (also at 5337) occurred last week but there was **no follow-through.** And now I'm wondering, "Is the PTI in the process of forming the 'right shoulder' of a huge head-and-shoulders top pattern?" . . . The A-D ratio on Feb. 19 came within a fraction of its October low, then bounced . . . Interesting statistic -- 90% of all equity mutual funds failed to keep up with the S&P last year. Same thing is happening here in 1999.

NEXT MAILING: Mar. 10, 1999